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# Wrestling with the Tar Baby: Ethical Obligations of Mississippi Insurance Defense Lawyers - Moeller v. American Guarantee & (and) Liability Insurance Co.

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# WRESTLING WITH THE TAR BABY: ETHICAL OBLIGATIONS OF MISSISSIPPI INSURANCE DEFENSE LAWYERS

*Moeller v. American Guarantee & Liability Insurance Co.*
No. 92-CA-00829-SCT, 1996 WL 532387 (Miss. Sept. 19, 1996)[1]

*J. Kevin Owens*

*"No man can serve two masters: for either he will hate the one and love the other, or he will be devoted to the one and despise the other."*[2]

## I. INTRODUCTION

Within the practice of law, there is no specialty more directly affected by conflict of interest problems than insurance defense.[3] Routinely, attorneys are retained by insurance carriers to defend their insureds, and there is no question that an attorney-client relationship exists between that attorney and the insured. The confusion is whether that same relationship exists between the insurer and the counsel it retains.[4] The source of much of this confusion is the dual client approach in which defense counsel is deemed to have two clients: the insurer and the insured.[5]

This confusion has recently been brought to light in *Moeller v. American Guarantee & Liability Insurance Co.*[6] In a case that will lead many lawyers to re-examine the relationship between insurers and defense counsel, and one which may ultimately spell the demise of insurance defense in Mississippi, the Mississippi Supreme Court adopted a dual client approach while at the same time placing upon the insurer the contractual obligation of affording the insured the opportunity to select his own independent counsel to protect his interests at the expense of the insurer.[7]

This Note analyzes two aspects of the *Moeller* holding: the contractual obligations of the insurance carrier, and the ethical obligations of the insurance carrier's retained attorney. These aspects will be examined in light of existing Mississippi law, including current Mississippi Rules of Professional Conduct, as well as trends established by other states and federal jurisdictions.

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1. As of the time this Note was written, this opinion had not been released for publication in the permanent law reports. Until released, it is subject to revision or withdrawal; however, it was decided *en banc* drawing no dissenting opinion as to the points that are the focus of this Note.

2. *Matthew* 6:24.

3. Karon O. Bowdre, *Conflicts of Interest Between Insurer and Insured: Ethical Traps for the Unsuspecting Defense Counsel*, 17 AM. J. TRIAL ADVOC. 101 (1993).

4. For a broader discussion of resolution of this confusion see Michael A. Berch & Rebecca W. Berch, *Will the Real Counsel for the Insured Please Rise?*, 19 Ariz. St. L.J. 27 (1987); Ronald E. Mallen, *Insurance Counsel: The Fine Line Between Professional Responsibility and Malpractice*, 45 INS. COUNSEL J. 244 (1978); Bowdre, *supra* note 3; Scott L. Machanic, *Insurance Defense Counsel: Who Is the Client?*, 43 FED'N OF INS. & CORP. COUNSEL QUARTERLY 45 (1992).

5. Robert E. O'Malley, *Ethics Principles for the Insurer, the Insured, and Defense Counsel: The Eternal Triangle Reformed*, 66 TUL. L. REV. 511 (1991).

6. No. 92-CA-00829-SCT, 1996 WL 532387 (Miss. Sept. 19, 1996)(*en banc*).

7. *Id.* at *7.

## II. FACTS AND PROCEDURAL HISTORY

American Guarantee and Liability Insurance Company [hereinafter American Guarantee] issued to the professional law corporation of Fuselier, Ott, McKee and Moeller, P.A., a special multi-peril policy.[8] This policy provided coverage and the right and duty of American Guarantee to defend personal injury claims.[9] Armin J. Moeller, a member of Fuselier, Ott, McKee and Moeller,[10] filed suit against that firm alleging that the defendants had "wrongfully discharg[ed] him, breach[ed] the employment agreement and stock redemption agreement, [made] fraudulent misrepresentations to get him into and also to breach the agreement, and damaging his reputation."[11]

Upon notification of this pending litigation, Fuselier, Ott and McKee requested that American Guarantee acknowledge coverage and retain Charles Brocato[12] to defend the suit on their behalf.[13] This initial request was denied; however, Brocato convinced American Guarantee that Moeller's claims were covered under the multi-peril policy. American Guarantee ultimately agreed to provide a defense under a reservation of rights,[14] but it refused to retain Brocato and instead opted to choose its own counsel.[15]

American Guarantee thus assumed the responsibility for the entire defense on behalf of Fuselier, Ott and McKee with the law firm of Heidelberg, Woodliffe and Franks which was employed and paid by American Guarantee.[16] As the litigation proceeded, Brocato, as counsel for Fuselier, Ott and McKee,[17] and Heidelberg, Woodliffe and Franks not only jointly defended Moeller's claim but also pursued a counterclaim against Moeller.[18]

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8. *Id.* at *1.

9. *Id.* at *2. Under the provisions of the multi-peril policy, personal injury was defined as:

> the publication or utterance of a libel or slander or of other defamatory or disparaging material, or a publication or utterance in violation of an individual's right to privacy; except publications or utterances in the course of or related to advertising, broadcasting or telecasting activities conducted by or on behalf of the name insured.

*Id.* at *2.

10. Moeller was fired by Louis A. Fuselier, president of the corporation, who notified him that his employment would be terminated effective May 30, 1982. *Id.* at *1.

11. *Id.*

12. When Fuselier, Ott and McKee incorporated, they retained the services of Charles Brocato, a lawyer specializing in taxation, to handle their corporate affairs. *Id.* at *3.

13. *Id.*

14. American Guarantee notified Fuselier, Ott and McKee of their position by letter stating:

> It appears there is or may be a question as to the position of the company for reasons of questions of coverage concerning the various allegations in the suit . . . . The purpose of this letter is to advise you that we will, at this time, proceed with the investigation, handling and defense of this case with a full reservation of our rights.

*Id.* Of the allegations alleged in Moeller's claim, it appears that only the misrepresentation, fraud, and damages to professional reputation claims were covered under the language of the policy. *Id.* All of the remaining allegations were outside the policy coverage. *Id.*

15. *Id.* at *4. American Guarantee retained the firm of Heidelberg, Woodliff & Franks to defend the claim. *Id.*

16. *Id.*

17. Brocato continued to represent Fuselier, Ott and McKee as the firm's own attorney, at the firm's expense. *Id.*

18. *Id.* at *3. This counterclaim alleged that Moeller "had began to solicit . . . the legal representation of clients of the association and had attempted to personally injure the reputation and goodwill of the association as well as [individual] reputations of Fuselier, Ott and McKee." *Id.*

Upon hearing this matter, the Special Chancellor found that "there had been a breach of the employment and stock redemption agreement and . . . the defendants had tortiously interfered with Moeller's business relations."[19] These facts served as the basis of the litigation between Moeller and Fuselier, Ott and McKee. The Chancellor's findings served as the basis of the subsequent litigation between American Guarantee and Moeller along with Fuselier, Ott and McKee.

Following the order of the Special Chancellor in the litigation between Moeller and Fuselier, Ott and McKee, American Guarantee filed a declaratory judgment action against the firm and Moeller[20] "seeking a declaratory judgment . . . that it had properly reserved its rights under the policy, and that it was not responsible for any portion of the judgment against the firm."[21]

In response to this action, Fuselier, Ott and McKee answered and counterclaimed seeking attorney's fees and expenses incurred in defending Moeller's claim.[22] Moeller also filed an answer and a counterclaim.[23] In rendering judgment on this matter, the Special Chancellor held that "as to Moeller's complaint . . . American Guarantee was obligated to defend . . . under the insurance policy, but was not obligated to indemnify the firm for any acts not covered by the policy."[24] Furthermore, the court held that American Guarantee acted properly in defending under a reservation of rights and thus fulfilled its duties under the policy and was not obligated to pay for the firm's defense.[25]

Upon appeal, the Mississippi Supreme Court held that when defending under a reservation of rights, a conflict of interests exists between the insurer and the insured and that in such a situation "not only must the insured be given the opportunity to select his own counsel to defend the claim, the carrier must also pay the legal fees reasonably incurred in the defense."[26] The court went on to define the ethical obligations of attorneys retained by insurance companies to represent the insured by applying a dual client model which deems the attorney to have two clients: the insured and the insurer, to each of which he owes a duty.[27]

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19. *Id.* at *1. On appeal, the Mississippi Supreme Court affirmed the holding as to breach of the employment and stock purchase agreement but reversed on Moeller's tort claim as to punitive damages, mental anguish, and attorney's fees. Fuselier, Ott and McKee v. Moeller, 507 So. 2d 63, 70 (Miss. 1987).

20. Although Moeller was named as a defendant in this lawsuit, no relief was sought from him. Moeller v. American Guar. & Liab. Ins. Co., No. 92-CA-00829-SCT, 1996 WL 532387, *4 (Miss. Sept. 19, 1996).

21. *Id.* at *4. American Guarantee also contended that four counts of Moeller's claim were not covered under the policy, and thus, they were not obligated to defend the parties on appeal of the judgment. *Id.*

22. *Id.* at *5. The fees for which Fuselier, Ott and McKee sought reimbursement were fees incurred by Brocato in regard to his involvement with the defense. *Id.*

23. *Id.* In his counterclaim Moeller sought actual damages, punitive damages, and attorney's fees incurred in the declaratory judgment action as well as costs associated with the defense of the counterclaim filed against him in the original litigation. *Id.* American Guarantee was aware that its policy covered Moeller; however, they did not notify him of this coverage, and it was only after the filing of the declaratory judgment action that Moeller learned of this coverage. *Id.* at *4-5.

24. *Id.* at *6.

25. *Id.* As to Moeller's counterclaim, the Special Chancellor ruled that American Guarantee did have a duty to defend Moeller against the counterclaim by Fuselier, Ott and McKee, as it was covered under the policy. *Id.* The court further found that Moeller's failure to notify American Guarantee of the counterclaim did not prevent recovery. *Id.* As to the punitive damage issue advanced by Moeller, the court denied recovery. *Id.*

26. *Id.* at *7.

27. *Id.*

## III. BACKGROUND AND HISTORY OF THE LAW

### *A. Current Mississippi Rules of Professional Conduct*

In 1986 the Mississippi Legislature adopted the current version of the Mississippi Rules of Professional Conduct, which are based primarily on the Model Rules of Professional Conduct as promulgated by the American Bar Association. The primary function of these rules is to protect the basic duties owed by the lawyer to his client: competence, confidentiality, and loyalty.[28] In an effort to combat the ethical problems of conflicts of interest in the "triadic" relationship between insurer, insured, and attorney, the Mississippi Rules espouse minimum standards which are designed not to avoid all conflicts, but merely to diminish their effects.[29]

Rule 1.7 squarely addresses conflict problems and provides that in a conflict situation "a lawyer shall not represent a client" unless he reasonably believes that the representation can be effectuated without adversely affecting the client and the client consents after consultation.[30] Furthermore, the hiring of an attorney by the insurer to represent the interests of the insured is sanctioned by Rule 1.8(f), with appropriate safeguards.[31] Rule 1.8(f) requires that an attorney accepting compensation from someone other than the client must at all times maintain his independent professional judgment and that he must protect confidential information.[32]

The language of the Mississippi Rules provides no guidance as to whether the dual or single client approach[33] is to be followed; however, the prevailing view among the jurisdictions that have adopted the Model Rules is that "*absent a conflict of interest* the defense attorney hired by the insurer represents both the insured and the insurer."[34] The persuasiveness of this prevailing view, however, is allayed in light of the interpretive opinions of the Mississippi Bar and the ABA Commission on Professional Ethics.[35]

In Formal Opinion 282 of the ABA Commission on Professional Ethics, the American Bar Association recognized that "the [insurance] company and the insured are virtually one in their common interest [the defeat of the third party's claim] however when the interests diverge the lawyer so employed shall represent the insured as his client with undivided fidelity."[36]

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28. *See* MISS. RULES OF PROFESSIONAL CONDUCT Rule 1.7 cmt. (1996); *see also* ABA Comm. on Professional Ethics and Grievances, Formal Op. 282 (1950)(essential point of ethics involved is that the lawyer so employed shall represent the insured as his client with undivided fidelity).

29. *See* MISS. RULES OF PROFESSIONAL CONDUCT Rule 1.7 & 1.8 (1996).

30. MISS. RULES OF PROFESSIONAL CONDUCT Rule 1.7. (1996).

31. MISS. RULES OF PROFESSIONAL CONDUCT Rule 1.8(f) (1996).

32. *Id.*

33. Under the single client approach, defense counsel's allegiance belongs solely to the insured as if he had retained the lawyer personally. John F. Larkin, *Ethical Considerations for Attorneys Acting as Insurance Defense Counsel*, PLI Litg. & Admin. Prac. Course Handbook series No. 518 (1995).

34. Bowdre, *supra* note 3, at 110 (emphasis added).

35. *See* ABA Comm. on Professional Ethics and Grievances, Formal Op. 282 (1950), Formal Interpretive Opinion No. 211 of the Mississippi Bar (Nov. 18, 1993).

36. ABA Comm. on Professional Ethics and Grievances, Formal Op. 282 (1950).

Closer to home, the Mississippi Bar, in Formal Interpretive Opinion number 211,[37] stated that "selected defense counsel owes a client a duty to exercise his or her independent legal judgment for the benefit of the insured. Defense counsel may not waive or ignore that obligation as a matter of law or ethics."[38] Thus, it appears that the single client approach maintains the weight of authority when defense counsel faces divergent interests of the insured and the insurer.[39]

### *B. State and Federal Case Law on Conflicts in the Triadic Relationship*

Primarily, most of the cases dealing with conflicts inherent in the "triadic" relationship originate in state courts because the insurance industry is largely regulated on a state-by-state basis, and attorneys' ethical obligations are defined by local rules.[40] Thus, in order to understand the implications of the *Moeller* holding as they relate to the ethical obligations of insurance defense lawyers and the contractual rights and duties of insurance carriers, it is necessary to look at the prevailing trends in other jurisdictions as compared to pre-existing law in Mississippi.

#### 1. Contractual Rights and Duties of Insurance Carriers

The relationship between the insurer and insured is a contractual relationship governed by the insurance policy.[41] Thus, the obligations and rights of the insurer will be determined pursuant to the terms of that agreement.[42] Speaking in contract terms, the insurer's promise to defend as well as indemnify is the consideration received by the insured for the payment of his premiums.[43] The insurer's primary obligation is the duty to defend the insured against third party claims. Generally this duty includes the right "to control the defense and to select counsel which the insurance company will pay to handle the defense."[44] This duty to defend, however, is broader than the insurer's duty to pay a judgment rendered against its insured.[45] Rather, "the duty . . . rests solely on whether the complaint alleges any facts or grounds which bring the action within the protection purchased."[46] Thus, the duty to defend creates an obligation on the part of the insurer "regardless of whether such suit is groundless, false, or fraudulent."[47]

In order to lessen their exposure under this absolute duty to defend, insurers will protect their policy defenses by defending under a reservation of rights. In such a situation the insurer defends the insured while reserving the right to later deny coverage. By doing so the insurer "may be able to avoid paying the under-

37. Formal Interpretive Opinion No. 211 of the Mississippi Bar (Nov. 18, 1993).
38. *Id.*
39. Larkin, *supra* note 33, at 395.
40. Larkin, *supra* note 33, at 383-84.
41. Larkin, *supra* note 33, at 385.
42. Federal Ins. Co. v. X-Rite, Inc., 748 F. Supp. 1223, 1226 (W.D. Mich. 1990) (holding that whether an insurer has a duty to defend is a function of the insurance contract).
43. Brohawn v. Transamerica Ins. Co., 347 A.2d 842, 850 (Md. 1975).
44. Bowdre, *supra* note 3, at 102-03.
45. United States Fidelity & Guar. Co. v. Louis A. Roser Co., 585 F.2d 932, 936 (8th Cir. 1978).
46. Curtis v. Nutmeg Ins. Co., 612 N.Y.S.2d 256, 258 (N.Y. App. Div. 1994) (citing Seabord Sur. Co. v. Gillette Co., 476 N.E.2d 272 (N.Y. 1984)).
47. Larkin, *supra* note 33 at 385.

lying claim either by succeeding in its defense of the insured or, failing that, by successfully asserting its policy defense."[48] However, if the insurer chooses to follow this path, his "desire to control the litigation must give way to its obligation to defend the insured."[49] This obligation obviously entails representation by an attorney "who can exercise professional judgment and devote complete loyalty to the insured regardless of the circumstances."[50] Thus, in such a situation the insurer will owe a special duty to the insured. Most jurisdictions take the approach that when defending under a reservation of rights, the insurer creates such a conflict of interest that he no longer has the right to control the aspects of the defense, and as such he should retain independent counsel[51] or in the alternative pay for counsel selected by the insured.[52]

Several courts have specifically bestowed upon the insured the right to select independent counsel at the expense of the insurer when such a conflict arises.[53] In *San Diego Navy Federal Credit Union v. Cumis Insurance Society*[54] [hereinafter *Cumis*], Cumis provided defense counsel for San Diego Navy Federal Credit Union, pursuant to their contract for insurance, to defend them in an action filed by a third party.[55] However, Cumis reserved the right to later deny coverage as to certain claims contained in the lawsuit.[56] Upon notification of this reservation of rights, the credit union retained independent counsel to protect its interests.[57] The trial court required Cumis to pay for the reasonable expenses of the credit union's retained independent counsel.[58]

From this judgment Cumis appealed to the California Court of Appeals arguing, pursuant to *Gray v. Zurich Insurance Co.*,[59] that they had satisfied their duty to defend by providing counsel and thus were not obligated to pay for independent counsel.[60] The court rejected that argument and distinguished Gray on the basis that "it [did] not address whether the scope of the duty to defend include[d] payment for the insured's independent counsel where a conflict of interest exists."[61] Expanding the scope of the insurer's contractual obligation to defend, the court stated:

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48. CHI of Alaska, Inc., v. Employer's Reinsurance Corp., 844 P.2d 1113, 1115 (Alaska 1993).

49. Federal Ins. Co. v. X-Rite, Inc., 748 F. Supp. 1223, 1227 (W.D. Mich. 1990).

50. *In re* Petition of Youngblood, 895 S.W.2d 322, 328 (Tenn. 1995).

51. The term "independent counsel" is not adequately defined in case law, but the general consensus is that it is counsel not involved "directly or indirectly with coverage issues." *Federal Ins. Co.*, 748 F. Supp. at 1228, n.1.

52. *See* Brooke Wunnicke, *The Eternal Triangle: Standards of Ethical Representation by the Insurance Defense Lawyer*, FOR THE DEFENSE Feb. 1989; *see also CHI*, 844 P.2d at 1117; *Federal Ins. Co.*, 748 F. Supp. at 1223.

53. *See* San Diego Navy Fed. Credit Union v. Cumis Ins. Soc'y, Inc., 208 Cal. Rptr. 494 (Cal. Ct. App. 1985); L&S Roofing Supply Co., v. St. Paul Fire & Marine Ins. Co., 521 So. 2d 1298 (Ala. 1987); *Federal Ins. Co.*, 748 F. Supp. at 1223; *CHI*, 844 P.2d at 1113; *see also* Todd R. Smythe, Annotation, *Duty of Insurer to Pay For Independent Counsel when Conflict of Interest Exists Between Insured and Insurer*, 50 A.L.R. 4th 932 (1986).

54. 208 Cal. Rptr. 494 (Cal. Ct. App. 1985).

55. *Id.* at 495.

56. *Id.*

57. *Id.* at 497.

58. *Id.* at 495.

59. 419 P.2d 168 (Cal. 1966).

60. San Diego Navy Fed. Credit Union v. Cumis Ins. Soc'y, Inc., 208 Cal. Rptr. 494, 499 (Cal. Ct. App. 1985).

61. *Id.* at 501.

> In a conflict of interest situation [here a reservation of rights] the insurer's desire to exclusively control the defense must yield to its obligation to defend its policyholder. Accordingly, the insurer's obligation to defend extends to paying the reasonable value of the legal services and costs performed by independent counsel, selected by the insured.[62]

In so expanding the duty to defend, *Cumis* impliedly stands for the proposition that any reservation of rights creates a conflict of interest, thus enabling the insured to select, at the insurer's expense, independent counsel.[63]

In the wake of this decision, courts from other jurisdictions began to apply the *Cumis* rule but quickly ascertained that it left many critical issues unresolved. The Supreme Court of Alabama, in *L&S Roofing v. St. Paul Fire & Marine Insurance Co.*, faced the issue of exactly when a conflict of interest should give the insured the right to select independent counsel at the expense of the insurer.[64] In this case, the court consented to answer a certified question from the United States District Court for the Northern District of Alabama as to whether a reservation of rights created such a conflict that the insured was justified in retaining independent counsel at the expense of the insurer.[65]

St. Paul Insurance Company, as insurer of L&S Roofing, provided defense counsel to defend an action filed against L&S in state court.[66] Subsequent to this appointment of counsel, St. Paul notified L&S that it was reserving its right to later disclaim coverage with respect to various allegations in the underlying action.[67] Upon receiving this notification, L&S through its individual attorneys made a demand upon the attorneys retained by St. Paul to allow L&S to retain, at the expense of St. Paul, independent counsel and to allow this counsel to have control of the defense of the underlying action.[68] This demand was denied.[69]

After this denial, L&S filed suit against St. Paul seeking declaratory and other equitable relief.[70] In its complaint L&S alleged that St. Paul's lawyers had a clear conflict of interest in continuing control of the underlying action because they were retained by St. Paul who had a "direct pecuniary interest" in resolving the litigation in a manner in which they could later disclaim coverage.[71]

In support of their position, L&S claimed that representation by attorneys appointed by St. Paul created an "unavoidable conflict of interest" even though there was no evidence showing any acts constituting an actual or objective conflict on the part of the St. Paul lawyers.[72] Thus L&S sought a judicial recognition

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62. *Id.* at 503.
63. Berch & Berch, *supra* note 4, at 33-34.
64. L&S Roofing Co. v. St. Paul Fire & Marine Ins. Co., 521 So. 2d 1298, 1301 (Ala. 1987).
65. *Id.* at 1298.
66. *Id.* at 1298-99.
67. *Id.* at 1300.
68. *Id.*
69. *Id.* In denying this demand, attorneys appointed by St. Paul agreed to keep counsel retained by L&S informed of the progress of the litigation but refused to pay for costs and expenses of that independent attorney if they decided to take an active role in the litigation. *Id.*
70. *Id.* This action was ultimately moved to federal court by petition of St. Paul. *Id.*
71. *Id.*
72. *Id.*

of a "presumptive conflict of interest."[73] St. Paul contended that there existed no such thing as a "presumptive conflict of interest" and that the lawsuit in question presented no such "actual conflict of interest" that would give rise to the necessity of independent counsel for L&S Roofing.[74]

In answering the certified question and adopting the position of St. Paul Insurance, the court stated that "[t]he mere fact that the insurer chooses to defend . . . under a reservation of rights does not ipso facto constitute such a conflict of interest that the insured is entitled at the outset to engage defense counsel of its choice at the expense of the insurer."[75] Instead, before the *Cumis* rule could be invoked, the court held that the insured had to establish the presence of an actual conflict of interest pursuant to the standards delineated by the Washington Supreme Court in *Tank v. State Farm Fire & Casualty*.[76] Only upon a showing that these standards were not complied with could an insured avail himself of the *Cumis* rule and retain independent counsel at the expense of the insurer.

Another critical question left unresolved by the *Cumis* decision deals with what comparative rights the insurer and insured have in the selection of independent counsel once a conflict sufficient to invoke that rule has been established. This issue was addressed in *Federal Insurance Co. v. X-Rite, Inc.*[77]

In *Federal Insurance*, X-Rite, Inc. was named as a defendant in a wrongful discharge lawsuit.[78] Upon service of the complaint, the firm currently representing X-Rite as corporate counsel undertook the litigation of the lawsuit.[79] After several communications between X-Rite and Federal Insurance, Federal acknowledged its duty to defend under the insurance policy as well as its unwillingness to pay the fees of the independent counsel retained by X-Rite.[80] Instead, Federal proposed the substitution of counsel retained to defend X-Rite in the underlying action.[81] These proposals were ignored by X-Rite, who continued the litigation under a defense provided by its own corporate counsel.[82] Eventually a mediation settlement was reached, and X-Rite demanded that Federal Insurance indemnify it in the amount of the settlement award as well as reimburse X-Rite in the amount of attorney's fees owed to its independent counsel.[83] Upon receipt of this demand, Federal filed a declaratory judgment action seeking a judicial declara-

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73. *Id.*
74. *Id.* at 1301-02.
75. Id at 1304.
76. *Id.* These standards required:

> First, the company must thoroughly investigate the cause of the insured's accident and the nature and severity of the plaintiff's injuries. Second, it must retain competent defense counsel for the insured. Both retained defense counsel and the insurer must understand that only the insured is the client. Third, the company has the responsibility for fully informing the insured not only of the reservation-of-rights defense itself, but also of all developments relevant to his policy coverage and the progress of the lawsuit.

Tank v. State Farm Fire & Cas. Co., 715 P.2d 1133, 1137 (Wash. 1986).
77. 748 F. Supp. 1223 (W.D. Mich. 1990).
78. *Id.* at 1224.
79. *Id.* at 1225.
80. *Id.*
81. *Id.*
82. *Id.*
83. *Id.*

tion that it was free from liability because "X-Rite breached the insurance contract by refusing to allow Federal to exercise its *right and duty to defend*."[84]

In responding to this action, the court held that Federal was liable for indemnification in the amount of the settlement award but was not liable for reimbursement of attorney's fees by stating that:

> Federal assumed the *'duty' to defend* X-Rite, in order to protect X-Rite's interests. Conjunctively, however, Federal reserved the *'right' to defend* X-Rite, in order to protect its own interests. Unless *'right to defend'* is to be deemed mere surplusage, which has not been argued, it must be viewed as conferring upon Federal some prerogative with respect to the defense beyond simply paying expenses. This prerogative cannot, in a conflict of interest situation, include an absolute right to control the litigation. On the other hand, X-Rite's apparent presumption that the conflict of interest, posing a potential of prejudice to its interests, automatically and completely negated all prerogative, is not reasonable.[85]

In so holding, the court deemed that there was a dichotomy between Federal's duty and Federal's right to defend.[86] The court stated that "right to defend" cannot mean "anything less than participation in selection of counsel, which contractual right ought to be enforced unless contrary to public policy."[87] The court thus adopted a middle ground approach which would require the insurer to "relinquish control of the litigation, but permits the insurer to select independent counsel."[88] Therefore the rule adopted by the court provided "adequate safeguards for the interests of both the insured and insurer," otherwise the contractual right reserved by Federal, namely the "right to defend," would have been totally abrogated.[89]

In *CHI of Alaska, Inc. v. Employers Reinsurance Corp.*[90] [hereinafter *CHI*], the Alaska Supreme Court faced both of these critical issues. In this case CHI was provided a defense under a reservation of rights by its liability insurer, Employers Reinsurance.[91] CHI objected to this defense by claiming that the reservation of rights "created a conflict of interest between Employers and CHI, and demanded independent counsel paid for by Employers and selected by CHI."[92] Employers rejected this contention, and CHI filed an action seeking a declaration that it was entitled to select independent counsel.[93] The trial court granted summary judgment in favor of Employers on this issue and CHI appealed.[94]

On appeal, the Alaska Supreme Court revisited the issue addressed in *L&S Roofing*, and held that defending under a reservation of rights did not automati-

84. *Id.* (emphasis added).
85. *Id.* at 1229 (emphasis added).
86. *Id.*
87. *Id.*
88. *Id.*
89. *Id.*
90. 844 P.2d 1113 (Alaska 1993).
91. *Id.* at 1114.
92. *Id.*
93. *Id.*
94. *Id.*

cally present a conflict of interest.[95] The court stated that "[i]f appointed counsel makes it clear . . . that he is going to be involved only in the defense of the liability claim, not in coverage issues, and that his client is the insured . . . conflicts should be rare."[96]

As to the comparative rights of the parties in selection of independent counsel, the court held that the insured has the right to select counsel without interference from the insurer.[97] This holding, however, was not without criticism, and in fact Justice Moore provided a different rule designed at striking a balance between the competing interests.[98] Under Justice Moore's formulation, the insured would be allowed the right of final approval of the insured's selection of independent counsel, but such approval could not be unreasonably withheld.[99]

2. Ethical Obligations of Insurance Defense Lawyers

Attorneys retained by insurers to represent their insureds are placed in an ethical dilemma of having potential, and possibly even actual, conflicts of interest.[100] This dilemma is augmented by the absence of clear standards with which attorneys can guide their conduct. As such, lawyers may be tempted to follow the adage warned of by the court in *CHI* that "[a] lawyer who does not look out for the carrier's best interest may soon find himself out of work."[101]

Local ethics rules do provide some guidance in this area, and ideally insurance defense lawyers should always evaluate their conduct according to these rules of professional conduct.[102] According to Rule 1.3, an attorney is bound to "act with reasonable diligence and promptness."[103] Furthermore, the attorney must also keep "[his] client reasonably informed about the status of [the lawsuit]"[104] as well as protecting confidential information "relating to representation of a client."[105]

Aside from these ethical standards, many courts have also adopted common law guidelines to deal with the pervasiveness of the ethical dilemma faced by insurance defense lawyers. In *Tank v. State Farm Fire and Casualty Co.*, the Supreme Court of Washington consolidated two cases on appeal to determine whether an insurance company defending under a reservation of rights had an enhanced obligation of fairness toward its insured.[106] Answering this question in the affirmative, the court established a distinct criteria which must be met by defense counsel retained by the insurer to represent that company's insured.[107]

95. *Id.* at 1116.
96. *Id.*
97. *Id.* at 1120.
98. *Id.* at 1122.
99. *Id.* (Moore, J., dissenting).
100. *In re* Petition of Youngblood, 895 S.W.2d 322, 327 (Tenn. 1995).
101. CHI of Alaska, Inc. v. Employers Reinsurance Corp., 844 P.2d 1113, 1117 (Alaska 1993).
102. Berch & Berch, *supra* note 4, at 40.
103. MISS. RULES OF PROFESSIONAL CONDUCT Rule 1.3 (1996).
104. MISS. RULES OF PROFESSIONAL CONDUCT Rule 1.4 (1996).
105. MISS. RULES OF PROFESSIONAL CONDUCT Rule 1.6 (1996).
106. Tank v. State Farm Fire & Cas. Co., 715 P.2d 1133, 1135 (Wash. 1986).
107. *Id.* at 1137-38.

Under this criteria, defense counsel, pursuant to Model Rule 5.4(c),[108] was required to exercise complete loyalty to their client and not allow "the employer [insurance company] to influence his or her professional judgment."[109] Secondly, defense counsel must always fulfill a duty of "full and ongoing disclosure to the insured," which requires disclosure of a "realistic and periodic assessment of the insured's chances to win . . . [and] all offers of settlement must be disclosed to the insured as those offers are presented."[110] If these distinct criteria are satisfied, the court held that the attorney would have discharged his enhanced duty of good faith under the reservation of rights.[111]

In addressing the presence of these duties, as well as to whom these duties are actually owed, a lawyer must first determine the identity of his client. As one commentator has stated:

> Even the most optimistic view of human nature requires us to realize that an attorney employed by an insurance company will slant his efforts, perhaps unconsciously, in the interests of his real client-the one who is paying his fee and from whom he hopes to receive future business-the insurance company.[112]

As such, most of the legal guidelines that have developed in the realm of insurance defense are based on the principle "that defense counsel generally cannot loyally and completely represent the insured in any situation when there is a conflict or potential conflict between the interests of the insured and the insurer."[113]

With this principle in mind, the law has developed the general rule, that absent a conflict of interest both the insured and insurer are clients because they are "virtually one in their common interest, that being the defeat of the third party's claim against the insured."[114] This rule proves satisfactory in most situations; however, when divergent interests arise in the triadic relationship the deficiencies of this rule become apparent.[115]

When these divergent interests do arise, the law has created two diametrically opposed views as to the identity of the actual client. Under the "single-client" approach, when a conflict arises, the insured is entitled to the attorney's undivided loyalty as if that attorney had been retained independently by the insured; that is to say the insured is the only client.[116] At the other end of the spectrum is the "dual-client" approach. This approach is geared primarily towards the "commu-

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108. Model Rule 5.4 (c) provides that " [a] lawyer shall not permit a person who recommends, employs, or pays the lawyer to render legal services for another to direct or regulate the lawyer's professional judgment in rendering such legal services." MODEL RULES OF PROFESSIONAL CONDUCT Rule 5.4(c) (1996).

109. *Tank*, 715 P.2d at 1137.

110. *Id.* at 1137-38.

111. *Id.*

112. O'Malley, *supra* note 5, at 515.

113. O'Malley, *supra* note 5, at 514.

114. ABA Comm. on Professional Ethics and Grievances, Formal Op. 282 (1950).

115. There are various conflicts that can arise in this area. Namely, the insurer may only go through the motions of providing a defense. Also, the insured might conduct the defense in a way that would make plaintiff's likelihood of success greater under the uninsured theory of liability. The insured may also learn of confidential information which it may later use against the insured to deny coverage. *See* CHI of Alaska, Inc. v. Employers Reinsurance Corp., 844 P.2d 1113, 1115 (Alaska 1993).

116. Larkin, *supra* note 33, at 388.

nity of interest" existing between the insured and insurer, and under this view the attorney is bound by applicable ethics rules to "protect the interests of both the insurer and insured."[117] As a natural implication of this rule, the insurer will maintain all the rights of a normal client in that he will have the right to demand loyalty, communication, and diligence from the retained attorney.[118]

As discussed previously, the necessity of implementing one of these approaches will not be triggered until an actual conflict of interest has been uncovered. Thus, the critical determination becomes the existence of a conflict.

Determining the existence of conflicts in the "triad" is as tricky as the nature of the relationship itself. In *Mitchum v. Hudgens*, the Supreme Court of Alabama, in an attempt to promulgate a standard for analyzing conflicts, stated that "whether a lawyer can fairly and adequately protect the interests of multiple clients . . . depends upon an analysis of each case."[119] As such, there are no clear guidelines within this area; however, individual jurisdictions have made an attempt at establishing standards.

In *Spindle v. Chubb/Pacific Indemnity Group*,[120] the California Supreme Court espoused a rule for conflict analyzation that is typical of most jurisdictions. The court stated that a "conflict of interest between jointly represented clients occurs whenever the common lawyer's representation of the one is rendered less effective by reason of his representation of the other."[121] Thus, in the words of one commentator, "the attorney should ask: Will my competent representation of one client on this issue be unfavorable to the other client?"[122]

These questions, however, will not always provide a clear indication of the existence of a conflict of interest; thus, many practitioners are advised to look for "conflict clues." These clues, which include reservation of rights and claims in excess of policy limits, should signal an attorney that a possible conflict exists such as to trigger the need for client identification.[123] Aside from these prevailing standards, the law of conflict analyzation is unaffected by custom and good intentions of the retained attorney. In *Employers Casualty v. Tilley*, the Supreme Court of Texas warned that "custom, reputation, and honesty of intention and motive are not the tests for determining the guidelines which an attorney must follow when confronted with a conflict."[124] Therefore, a retained insurance defense lawyer cannot hide behind the cloak of good intentions in an effort to escape conflicts of interest.

By applying these standards of conflict analyzation, attorneys should be able to uncover most conflicts of interest, and upon this discovery the usually harmo-

117. Larkin, *supra* note 33, at 387.
118. Larkin, *supra* note 33, at 387.
119. Mitchum v. Hudgens, 533 So. 2d 194, 200 (Ala. 1988).
120. 152 Cal. Rptr. 776 (Cal. 1979).
121. *Id.*
122. Bowdre, *supra* note 3, at 108-09.
123. Charles Silver & Kent Syverud, *The Professional Responsibilities of Insurance Defense Lawyers*, 45 DUKE L.J. 255 (1995).
124. Employers Cas. v. Tilley 496 S.W.2d 552, 558 (Tex. 1973).
125. O'Malley, *supra* note 5, at 515.

nious dual client approach is disrupted.[125] At this point it becomes necessary to identify the actual client in order to adequately protect the interests of both the insured and the insurer. To assist in this determination, the law has provided the two competing views previously presented, each with its own distinct advantages and disadvantages.

The prevailing trend throughout the American judicial system is the single client approach under which "the insurance defense lawyer's ethical duty of undivided loyalty to the client is owed to the *insured*."[126] Thus, upon the discovery of a conflict, the insured becomes the sole client.

In an attempt to define the contours of the single client approach, the Arizona Supreme Court, in *Parsons v. Continental National American Group*, espoused the rule that a lawyer owes undivided fidelity to the insured, even though retained by the insurer.[127] In *Parsons*, the court was required to make a determination as to whether an insurer could be estopped from denying coverage in a subsequent garnishment action when its defense was based upon confidential information received by the carrier's attorney from the insured during the course of representation in the underlying tort action.[128] The insured argued that the insurer should not be allowed to deny coverage based on information obtained by the attorney, because by doing so the company would be "[taking] advantage of the fiduciary relationship between its agent [the attorney] and [the insured]."[129]

In agreeing with the insured, the court rendered one of the landmark rulings in the area of insurance defense by stating that "an attorney that represent[s] the insured at the request of the insurer owes undivided fidelity to the insured, and therefore, may not reveal any information or conclusions derived therefrom to the insurer that may be detrimental to the insured in any subsequent action."[130]

In *Carrier Express, Inc. v. Home Indemnity Co.*,[131] the District Court for the Northern District of Alabama confronted a textbook example of a conflict of interest in the "triadic relationship" dealing with an insurer's bad faith refusal to settle within the policy limits. In defining the nature of the association between the insured, insurer, and retained attorney, the court adopted the single client approach stating that "[b]oth the retained defense counsel and the insurer must understand that only the insured is the client . . . [and that] an insurance company must refrain from engaging in any action which would demonstrate a greater concern for the insurer's monetary interest than for the insured's financial risk."[132]

In further support of the single client approach, the American Bar Association, in Ethics Opinion 282,[133] has stated that the "essential point of ethics involved is that the lawyer so employed shall represent the insured as his client with undivided fidelity."[134] As such, it appears that the single client has a great weight of

126. Wunnicke, *supra* note 52.
127. Parsons v. Continental Nat'l Am. Group, 550 P.2d 94, 97 (Ariz. 1976).
128. *Id.* at 96.
129. *Id.* at 97.
130. *Id.*
131. 860 F. Supp. 1465 (N.D. Ala. 1994).
132. *Id.* at 1480.
133. ABA Comm. on Professional Ethics and Grievances, Formal Op. No. 282 (1950).
134. *Id.*

authority behind it when a retained attorney faces divergent interests of insured and insurer.

In spite of the authority supporting the single client approach, many jurisdictions have adopted the increasingly popular rule that "insurance defense counsel is deemed to have two clients in any given case: the insurer and the insured."[135]

In *Lieberman v. Employers Insurance*, as a result of a settlement of a medical malpractice claim which was against the defendant physician's wishes, the physician filed suit against the insurer for breach of contract and against the retained attorney for breach of fiduciary duty arising from the attorney-client relationship.[136] In addressing this claim, the court adopted the dual client approach by holding that a retained attorney "owes to both a duty of good faith and due diligence in the discharge of his duties, the rights of one cannot be subordinated to those of the other."[137] Thus, the court attempted to strike a balance between the competing interests by establishing a rule that placed equal weight upon both interests such that if counsel believed that it could not discharge its duties to the insured without conflicting with discharge of its duties to the insurer, then counsel should not represent both.[138] As such, the rule favored neither interest but instead bestowed upon each the interests of co-clients.

With the recognition of the existence of an attorney-client relationship between the insurance company and the retained attorney with regard to disqualification, New Jersey has adopted the principles of the dual client approach. In *Gray v. Commercial Union Insurance Co.*, the insurance company moved to disqualify an attorney and his firm from representing a plaintiff in a suit against the insurance company for breach of an employment contract.[139] The basis for their removal was the fact that the attorney had been retained numerous times to represent their insureds in personal injury litigation.[140] Thus, the insurance company claimed that the lawyer was barred by Model Rule DR 4-101 from bringing a suit against a former client.[141] The superior court denied Commercial Union's motion for disqualification, and they timely appealed.[142]

On appeal, the appellate division, reversing the denial and disqualifying the attorney, held that an attorney-client relationship did exist and that all other requirements to establish disqualification had been met.[143] The primary reason for this disqualification was the existence of the attorney-client relationship based upon the dual client approach in which the court recognized that "there is no dispute that as a fundamental proposition a defense lawyer is counsel to both the insurer and insured."[144] Thus, the lawyer was deemed to have represented the company in the personal injury litigation even though his primary function was

135. O'Malley, *supra* note 5, at 511.
136. Lieberman v. Employers Insurance, 419 A.2d 417 (N.J. 1980).
137. *Id.* at 424 (citing Imperiali v. Pica, 156 N.E.2d 44,47 (Mass. 1959)).
138. *Id.* at 424-25.
139. Gray v. Commercial Union Insurance Co., 468 A.2d 721 (N.J. 1983).
140. *Id.* at 723.
141. *Id.* at 724.
142. *Id.*
143. *Id.* at 729.
144. *Id.* at 725.

to protect the interests of the insured in the underlying action.

In dealing with an action by an insured against his insurance company's retained attorney for settling a dispute without his permission, the Supreme Court of Alabama applied dual client principles.[145] In *Mitchum v. Hudgens*, the attorney was retained by a liability insurance carrier to represent Mitchum in a medical malpractice claim.[146] This lawsuit was eventually settled prior to trial without permission from the defendant physician, who subsequently filed an action against the attorney claiming fraud and negligence in that representation.[147]

At the trial court level, Mitchum's Motion for Summary Judgment was denied, and in affirming this denial the Supreme Court of Alabama held that "when an insurance company retains an attorney to defend an action against an insured, the attorney represents the insured as well as the insurance company in *furthering the interests of each*."[148]

A previously unaddressed issue in the "triadic relationship" deals with the problematic implications that will arise if a malpractice claim is contemplated. If the single client approach is followed, the non-client insurer will be left with no recourse since the existence of a legal malpractice claim is based on an attorney-client relationship. In the absence of such a relationship, there is no basis for a malpractice claim.[149]

In *Atlanta International Insurance Co. v. Bell*, the Michigan Court of Appeals was faced with just such an issue. In this case the plaintiff insurance company filed a legal malpractice claim against their retained attorney regarding his defense in an action brought against one of Atlanta International's insureds.[150] The circuit court granted summary judgment in favor of the attorney on the basis of an absence of an attorney-client relationship between the insurer and the retained attorney, and Atlanta International appealed.[151] On appeal the court of appeals affirmed the summary disposition and agreed with the circuit court that there was no attorney-client relationship and thus no basis for a legal malpractice claim.[152] In so holding, the court of appeals stated that "[n]o attorney-client relationship exists between an insurance company and the attorney representing the insurance company's insured . . . and the fact that the insurance company pays the bill will not affect that relationship and duty is owed only to the insured."[153] This left the insurer with no recourse even though his financial interest is clearly at stake.

Recognizing the troublesome nature of the court of appeals holding, the Supreme Court of Michigan ultimately modified the holding of *Bell* to allow the

145. Mitchum v. Hudgens, 533 So. 2d 194 (Ala. 1988).
146. *Id.* at 195.
147. *Id.* at 196.
148. *Id.* at 198 (emphasis added).
149. GEOFFREY C. HAZARD, JR, & W. WILLIAM HODES, THE LAW OF LAWYERING: A HANDBOOK ON THE MODEL RULES OF PROFESSIONAL CONDUCT § 1.7:303 (1996 Supp.).
150. Atlanta Int'l Ins. Co. v. Bell, 448 N.W.2d 804 (Mich. Ct. App. 1989).
151. *Id.*
152. *Id.*
153. *Id.* at 805.

insurer to maintain a malpractice action under the theory of equitable subrogation.[154] In so doing, the court gave judicial recognition to the fact the "relationship between the insurer and the retained defense counsel, while less than an attorney-client relationship, unquestionably differs from the relationship between a defense counsel and a party-opponent."[155] Accordingly, the court held that due to the merging of interests of the insured and insurer in dealing with a malpractice claim against a retained attorney, the doctrine of equitable subrogation would permit a malpractice action under the facts presented.[156]

Since the insurer's financial interest is so clearly at stake, it seems illogical to leave it with no remedy in cases of malpractice.[157] As such, the dual client approach attempts to protect the interest of the insurer by bestowing upon him the classification of a co-client. This balancing of interests is typified in *Unigard Insurance v. O'Flaherty & Belgum*.[158] Here, an insurer filed a legal malpractice claim against its retained attorney which was summarily dismissed by the California Superior Court.[159] On appeal, Unigard argued that an attorney-client relationship did exist, and thus they had standing to bring a legal malpractice claim.[160]

In agreeing with Unigard and reversing the superior court's dismissal, the court of appeals held that "the retained attorney owes a duty of care to the insurer which will support its individual right to bring a legal malpractice action against the attorney for negligent acts committed in the representation of the insured."[161] To hold otherwise, the court held, "would place the loss for the attorney's misconduct on the insurer. The only winner produced by an analysis precluding liability would be the malpracticing attorney."[162] Thus, the malpractice implications of the "triadic relationship" are as problematic as the nature of the relationship itself.

### *C. Mississippi Case Law on Conflicts in the Triadic Relationship*

Prior to the *Moeller* holding, there was scant case law in Mississippi with which to guide insurance defense lawyers through the intricacies of the "triadic relationship;" however, existing case law did provide a basic framework.

#### 1. Contractual Rights and Duties of Insurance Carriers

Following the principles established by other jurisdictions, Mississippi follows the rule that "the primary consideration in evaluating an insurer's duty to defend is whether the pleadings allege a claim within the scope of coverage of the insurance policy."[163] Thus, as with other jurisdictions, the basis of the duty is depen-

154. Atlanta Int'l. Ins. Co. v. Bell, 475 N.W.2d 294 (Mich. 1991).
155. *Id.* at 297.
156. *Id.* at 295.
157. HAZARD & HODES, *supra* note 149.
158. 45 Cal. Rptr.2d 565 (Cal. Ct. App. 1995).
159. *Id.* at 566.
160. *Id.* at 567.
161. *Id.* at 568.
162. *Id.*
163. Ezell v. Hayes Oilfield Constr. Co., 693 F.2d 489, 493 (5th Cir. 1982); *see also* Southern Farm Bureau

dent upon the allegations of the complaint and not the ultimate liability of the insurer.

*Employer's Reinsurance Corp. v. Martin, Gordon & Jones, Inc.*[164] lays out with specificity the insurer's contractual obligations in an insurance defense situation. As to the insurer's ultimate duty to defend, the court applied the general rule that the duty is determined according to the allegations pled in the third party's complaint.[165] Aside from this determination, the court also approved of the insurer's right to proceed under a reservation of rights when coverage issues arose.[166]

Aside from these rights and duties, there were no other obligations imposed upon insurers, and prior to *Moeller* there was no right to independent counsel on behalf of the insured in cases of conflicts. Instead, the insured's only right was to "demand that the insurer assume the defense under a reservation of rights."[167]

2. Ethical Obligations of Retained Attorneys

Prevailing Mississippi law stands for the proposition that "[t]here is no higher ethical duty in the legal profession than complete, absolute fidelity to the interest of the client . . . [and thus] an attorney obviously should not attempt to represent a party when he is obligated to represent an adverse interest, and a conflict of interest appears."[168] Prior to the *Moeller* holding, Mississippi insurance defense lawyers sought guidance from the Mississippi Supreme Court's holding in *Hartford Accident & Indemnity Co. v. Foster*.[169] In *Hartford* the court dealt with an action brought by an insured against their insurer for bad faith refusal to settle within the policy limits and breach of fiduciary duty.[170] The circuit court granted a summary disposition in favor of the insured, and Hartford appealed.[171]

In addressing this case, the supreme court was faced with defining the nature of the duties owed by retained counsel in the insurance defense practice. In answering this question, the court held "[Mississippi] jurisprudence accords with the majority view that the insurer is the champion of the insured's interests [and that] the interests of the insured are paramount to those of the insurer."[172] In so holding, the court adopted the single client approach in that "there can be no question but that the lawyer owes his client [the insured] absolute loyalty, and is required to devote his professional ability solely in the interest of that client."[173]

## IV. *Moeller v. American Guarantee & Liability Insurance Co.*

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Ins. Co. v. Logan, 119 So. 2d 268 (Miss. 1960) (holding that an insurer's ultimate liability is not the criterion for determining whether the insurer is obligated to defend).

164. 767 F. Supp. 1355 (S.D. Miss. 1991).

165. *Id.* at 1359.

166. *Id.* at 1363.

167. *Ezell*, 693 F.2d at 494.

168. State Farm Auto Ins. Co. v. Commercial Union Ins. Co., 394 So. 2d 890, 894 (Miss. 1981).

169. 528 So. 2d 255 (Miss. 1988).

170. *Id.* at 262-63.

171. *Id.*

172. *Id.* at 265.

173. *Id.* at 268.

174. Moeller v. American Guar. & Liab. Ins. Co., No. 92-CA-00829-SCT 1996 WL 532387 *9 (Miss. Sept. 19, 1996).

In seeking reimbursement from American Guarantee, Fuselier, Ott and McKee filed an action in chancery court seeking a judicial declaration as to the nature of American Guarantee's duties under the liability policy.[174] Primarily, they wanted the court to award the attorney fees associated with payment of the independent counsel retained by them to assist in the defense of Moeller's claim.[175] The Mississippi Supreme Court recognized early that an ultimate determination of this issue focused not solely on the language of the policy but also included a problematic examination and determination of the relative contractual and ethical obligations of American Guarantee and its retained attorney.[176] In an effort to resolve this dispute, as well as to shed some light on the ethical dilemmas of insurance defense lawyers, the court promulgated standard guidelines to assist Mississippi insurance defense lawyers as they navigate the "triadic relationship."[177]

Initially, the court recognized American Guarantee's contractual obligation to provide a legal defense against Moeller's claim, as it was clearly covered under the provisions of the policy.[178] As such, the court applied the general rule that the insurer's duty to defend is contingent upon the allegations in the complaint.[179]

Aside from this duty to defend, the court also recognized that American Guarantee had relative rights under the contract for insurance, specifically the right to select the attorney to defend the claim.[180] The basis for the recognition of this right was the fact that American Guarantee would be ultimately liable for any judgment rendered in the action.[181] As such, the court provided that American Guarantee's contractual obligations included the duty to provide a legal defense for claims covered under the policy as well as a duty to pay all amounts that their insureds became obligated to pay.[182]

The court recognized that where insurers assert policy or coverage defenses and provide a defense under a reservation of rights, various conflicts of interest arise,[183] such that an insurer should be charged with an enhanced obligation under the policy.[184] To deal with this problem, the court followed the rule applied in other jurisdictions that "when defending under a reservation of rights . . . a special obligation is placed upon the insurance carrier . . . [in that] not only must the insured be given the opportunity to select his own counsel to defend the claim, the carrier must also pay the legal fees reasonably incurred in the defense."[185] Thus, the Mississippi Supreme Court relied on the holdings of other jurisdictions to apply the *Cumis* rule, which was previously non-existent in

175. *Id.*
176. *Id.* at *8.
177. *Id.*
178. *Id.*
179. *Id.*
180. *Id.*
181. *Id.*
182. *Id.*
183. *Id.* at *9; *see also supra* note 115 and accompanying text.
184. *Id.*
185. *Id.*
186. *Id.*
187. *Id.* at *7.

Mississippi jurisprudence, such that now Mississippi law provided that when defending under a reservation of rights, the insurer has an enhanced duty under which he must provide, at his expense, independent counsel.[186]

In addition to expanding the insurer's contractual duties under the liability policy, the court went on to define the guidelines governing the conduct of the attorney retained by the insurance carrier.[187] The Mississippi Supreme Court, in *Moeller*, explicitly adopted the dual client approach by holding that the retained attorney has a professional and ethical obligation to represent both the insurance company and the insured, thus having two separate and distinct clients.[188] Under this approach, the court recognized the potential for conflict and accordingly charged the retained attorney with ascertaining, at the time he is offered the case by the carrier, if there is any possibility of conflicting interests.[189] If there is such a possibility, the court held that the attorney should only accept representation of the insurer for the portions of the claim covered by the policy, and in accordance with the previously announced adoption of *Cumis*, the insurer should provide the insured with the opportunity to select independent counsel to protect his interests.[190]

In applying these guidelines to effectuate a resolution of the claims advanced by Fuselier, Ott and McKee, the court held that it was the professional obligation of American Guarantee's retained attorney to recognize the existence of two conflicts of interest, namely the fact that the defense was provided under a reservation of rights and that as defense counsel he was attempting to represent both parties in defending all claims when only one was covered by the policy.[191] With the presence of these conflicts, the court held that American Guarantee became obligated to allow the insureds to select independent counsel to ensure protection of their individual interests.[192] Accordingly, the Mississippi Supreme Court held that American Guarantee was obligated to reimburse Fuselier, Ott and McKee for fees incurred in their defense of the complaint.[193]

## V. ANALYSIS

Mississippi's adoption of the dual client approach places it, along with other jurisdictions, in a position of following a policy that is "unsound as a matter of policy, law, and legal ethics."[194] In order to understand the disadvantages as well as the legal implications created by the court's decision in *Moeller*, it is necessary to examine each one independently.

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188. *Id.*
189. *Id.* at *10.
190. *Id.*
191. *Id.*
192. *Id.*
193. *Id.*
194. O'Malley, *supra* note 5, at 512.
195. Moeller v. American Guar. & Liab. Ins. Co., No. 92-CA-00829-SCT, 1996 WL 532387 at *9 (Miss.

### *A. Duty of Insurance Carrier*

The rules promulgated by the court, as they relate to the contractual obligations of the insurance carrier, are not surprising, and in fact are in accordance with the majority trends of other jurisdictions. The problems arise due to the manner in which the court seeks to implement these rules.

Prior to *Moeller* there was no provision for *Cumis* counsel within Mississippi jurisprudence;[195] thus, *Moeller* establishes the guidelines by which this new rule should be applied. In providing these guidelines, the Mississippi Supreme Court espoused a general rule that when defending under a reservation of rights, the carrier is obligated to allow the insured to select independent counsel.[196] As was recognized by the Alabama Supreme Court, this rule goes too far by simply requiring a reservation of rights defense before independent counsel is required. Instead, the more reasoned approach would be to allow the reservation of rights to function as a conflict clue to signal a possible conflict of interest but requiring an actual conflict before invoking the duty to provide independent counsel.[197]

In the absence of adopting such a reasoned approach, the Mississippi Supreme Court has treated the insurer with "disdainful indifference reserved for a client's adversary" by completely abrogating its contractual rights under the policy.[198] The *Moeller* court clearly recognized the insurer's financial stake in the litigation and their corresponding right to select defense counsel to protect that interest.[199] The rule adopted by the court, however, ignores that right by bestowing upon the insured the ultimate right to select independent counsel in situations of conflict without any input from the insurer. This rule thus ignores the contractual rights and financial interests of the insurer.

Notwithstanding this shortcoming of the *Moeller* holding it does have one redeeming quality. That is by adopting the dual client approach it creates an attorney-client relationship between the insurer and retained attorney such as to provide standing for an independent claim of legal malpractice on behalf of the insurer.

### *B. Duties of Insurance Carrier's Attorney*

The decision in *Moeller*, as it applies to the ethical obligations of insurance defense lawyers, is clearly in direct conflict with earlier Mississippi law. Prior to *Moeller*, *Hartford* was the prevailing rule regarding the "triadic relationship," and it provided that "the company was not the client. The insured was the client."[200] Therefore, *Hartford* applied the single client approach in that the "interests of the insured are paramount to those of the insurer."[201] Aside from

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Sept. 19, 1996).

196. *Id.* at *10.

197. L&S Roofing Supply Co. v. St. Paul Fire & Marine Ins. Co., 521 So. 2d 1298 (Ala. 1987).

198. O'Malley, *supra* note 5, at 512.

199. *Moeller*, 1996 WL 532387 at *8.

200. Tom Bourdeaux, *Undivided Loyalty*, THE MISSISSIPPI LAWYER, Jan.-Feb. 1996, at 24-27 (citing Hartford Accident & Indem. Co. v. Foster, 528 So. 2d 255 (Miss. 1988)).

201. *Hartford Accident & Indem. Co.*, 528 So. 2d at 265.

202. Formal Interpretive Opinion No. 211 of the Mississippi Bar (Nov. 18, 1993).

*Hartford*, the ethical opinions of the Mississippi Bar also clearly adopted the single client approach by holding that "selected defense counsel owes a client a duty to exercise his or her independent legal judgment for the benefit of the insured. Defense counsel may not waive or ignore that obligation as a matter of law or ethics."[202]

Aside from this direct conflict with existing law, the dual client approach as adopted by Mississippi, will also prove to be problematic in its implementation. The Mississippi Supreme Court, prior to *Moeller*, in *Hartford*, recognized that the "triadic relationship" was a difficult situation, stating that "[i]n sum, the ethical dilemma thus imposed upon the carrier employed defense attorney would tax Socrates, and no decision or authority . . . furnishes a completely satisfactory answer."[203] However, the rule announced in *Moeller* will do nothing to clear up the confusion in this area but will instead create a great many more problems than it actually resolves.[204]

The first problem in the implementation of this holding relates to problems associated with identifying conflicts. The *Moeller* holding provides that "counsel must be careful at the time he is asked to represent the insurance carrier and the insured, and if there is any reason indicating a possible conflict of interest . . . he should under no circumstances undertake to represent them both."[205] The problems arise in attempting to answer the question: how inevitable must the possibility of a conflict be before it will preclude representation? The *Moeller* rule provides no guidance in this area. Thus attorneys may be reluctant to accept representation of this nature because of the uncertainty that a conflict will later arise which will preclude representation since the insured will be allowed to select independent counsel.

In a somewhat ironic fashion, the *Moeller* holding also creates an increase in the cost of insurance defense because in any reservation of rights defense the insurer will have to provide two attorneys: one to protect the interest of the insurer for the claims covered under the policy, and one for the insured to protect its interests. The *Moeller* holding specifically provides that if a possible conflict is present an attorney "should undertake to represent only the interest of the insurance carrier for the part covered, and the insurance carrier should afford the insured ample opportunity to select his own independent counsel to look after his interest."[206] This gives rise to the possibility of the necessity of two lawyers from the start of every defense. This cost could eventually become so high that insurance companies will no longer be able to provide legal defenses under their policies and thus severely curtail the Mississippi insurance defense practice.

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203. *Hartford Accident & Indem. Co.*, 528 So. 2d at 273.

204. For a detailed list of problems that arise in employing the dual client approach, see O'Malley, *supra* note 5, at 515.

205. Moeller v. American Guar. & Liab. Ins. Co., No. 92-CA-00829-SCT, 1996 WL 532387, *7 (Miss. Sept. 19, 1996).

206. *Id.* at *8.

## VI. CONCLUSION

As one commentator has stated, "being caught in the middle between the insured and the insurer when a conflict of interest exists is much like wrestling with the proverbial tar baby. Every effort to extract a limb results in entanglement of another. Loyalty to one client contravenes the ethical obligations owed to the other."[207] The Mississippi Supreme Court, in an effort to combat the problems of the "triadic relationship" and provide a set of standards to govern attorney conduct, has jumped headlong into this battle with the tar baby. Their decision, although it solves many problems, creates a great many more that will now plague the courts as practitioners attempt to implement this holding. There is no doubt that Mississippi needs a predictable way to ensure loyalty to insureds; however, the dual client approach as promulgated in *Moeller* is not a satisfactory solution.

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207. Bowdre, *supra* note 3 at 149.